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The Bailout Briar Patch

By Kimberly Strassel
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One problem with rolling is that it can be hard to stop. That's the Bush administration's challenge, as congressional Democrats try to flip it into another economic intervention -- this one a giant housing bailout.

Marshaling this campaign is House Financial Services chief Barney Frank and Senate Banking head Chris Dodd, who see (excuse the pun) a prime opportunity for more government regulation, as well as election-year credit for helping homeowners. The duo proposes the government step in to insure at-risk loans, at a potential cost of hundreds of billions of dollars to taxpayers. Democrats explain that this is nothing more than "Stimulus, Part Two."

For that jab, the administration has only itself to blame. Whatever Stimulus Part One's economic merits, the Democrats' chief takeaway from that \$150 billion experience was that the administration was running scared of the political fallout from today's housing mess. Scared enough to set aside good ideas -- say, making permanent the Bush tax cuts -- in favor of Democratic demands. Scared enough to cave to future pressure.

The administration's soothing words to conservative economists back then was that this package would forestall greater and worse political intervention down the road. In fact, as the financial situation has deteriorated -- which should've been expected -- the White House has had to do yet more intervening. The latest was Treasury Secretary Hank Paulson's engineering of a rescue for investment bankers via Bear Stearns.

All this neatly set things up for Democrats, who are now claiming that if the White House is worried enough to prop up Wall Street, it has a downright obligation to prop up Main Street. Presumably Mr. Frank wants a better deal for homeowners than what got handed to Bear Stearns shareholders, but never mind.

To its credit, the White House has so far resisted. It batted down a proposal to have the government buy housing stock, on the correct grounds that the market needs to clear itself. It promised a veto of changes in bankruptcy law, on the correct grounds that this would drive up interest rates for future borrowers. In an interview with CNBC's Larry Kudlow last week, President Bush put the damper on the latest plan to insure underwater loans, presumably on the correct grounds that anything Mr. Frank came up with was worrisome: "Listen, I'm open to new ideas, but I'm not open to ideas that'll make it harder for the market to recover. What we need is - for the market to work its way through," he said.

Working in Mr. Bush's favor is that he's right. It was a housing problem that initially kicked off today's housing finance problem, but the two issues remain distinct. All the evidence suggests

the housing market itself is on the slow road to correction. Housing prices are sticky, so this will take some time, but eventually the market will clear. Government can only get in the way.

The question of struggling mortgage holders meanwhile remains the same today -- even with recent financial turmoil -- as it did last year when policy makers started worrying about resets and foreclosures. At the time, the administration made a clear distinction between the few individuals who may have been hit with predatory lending -- and the vast majority who either speculated or signed up for an unaffordable home. Its solution was a program in which mortgage servicers and lenders would voluntarily reduce or freeze the interest rates of certain subprime borrowers. Workouts are now on the rise, and experts say the worst subprime defaults are over.

The White House knows a bailout now would land it back in a briar patch: Who qualifies for help? Since it is impossible to craft legislation that targets only a victimized few, Democrats will cut checks for everyone, which means the White House would be underwriting shoddy financial planning by some middle-class homeowners. This won't sit well with millions of others who went for that boring 30-year fixed, or are working two jobs to make their payments -- as their McMansion neighbors sign up for the government-mortgage-dole.

A bailout also puts the administration in the unwanted position of favoring yesterday's unwise borrowers over tomorrow's future homeowners. Federal Reserve head Ben Bernanke -- not content with simply taking his own institution into weird and uncharted territory -- recently piped up in favor of more government mortgage help. His worry was that Americans might walk away from homes that are now worth less than their mortgages. This is the basis of the Frank proposal, which would require lenders to write down loans to match home values as a condition of getting government help.

But the only question for policy makers (if there even is one) is whether a borrower can continue to pay the mortgage he has signed up for -- whatever the underlying value. If house prices continue to fall, there's no guarantee homeowners won't continue to walk away from even government-insured mortgages -- leaving taxpayers with the bill. Mr. Frank's proposal would also be a straight shot to higher fees and interest rates for future borrowers, since lenders will want to bake in the risk that they might again be forced into writedowns. This won't do much to get people to purchase empty homes.

Democrats are looking for any nod here. If they can get Mr. Bush to agree even in principle to some form of government relief, they can stuff a bill full of other market-gumming restrictions. They can also crow that they pushed the White House into finally helping homeowners.

Having failed to get that Bush nod so far, they are ginning up pressure with a whisper campaign suggesting the administration is secretly coming around to a deal. There's no evidence to suggest that's true -- yet. As Congress returns from Easter break, the focus will pivot to congressional Republicans, in hopes that election nerves will cause enough to bolt to the Democratic plan to bring the White House along.

Mr. Bush has made the broad case for standing back on most congressional proposals, and he's been right. But until he draws more specific lines on mortgage relief, Democrats will continue to scatter proposals for government rescue across the Capitol, and up the pressure on Republicans to sign up for at least one. This is the time to stop the roll.

